LOAN GRANTING AND ITS RECOVERY PROBLEMS ON COMMERCIAL BANKS (A CASE STUDY OF FIRST BANK PLC, OJO-ALABA BRANCH)

BY

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REG. NO. BF/2008 /113

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CARITAS UNIVERSITY AMORJI-NIKE EMENE
ENUGU STATE

AUGUST, 2012

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BEING A PROJECT REPORT SUBMITTED TO THE DEPARTMENT OF BANKING AND FINANCE FOR THE PARTIAL FULFILMENT OF THE AWARD OF BACHELOR OF SCIENCE (B.Sc) DEGREE IN BANKING AND FINANCE.

DEPARTMENT OF BANKING AND FINNACE
FACULTY OF MANAGEMENT AND SOCIAL SCIENCE

CARITAS UNIVERSITY
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ENUGU

AUGUST, 2012.

APPROVAL

This research work was read and for meeting the requirements as recommended for the award of the B.Sc degree in Banking and Finance Caritas University Amorji–Nike, Enugu.

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MR. Nwadiubun Anthony Date

(Project supervisor)

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MR I.G Okafor Date

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Dr. J.U.J. Onwumere Date

(External Examiner)

CERTIFICATION

I, Anioke Chisom N. an undergraduate student of Banking and finance with Reg. No Bf/2008/113 have submitted this project report as my original work and has not been submitted in part or full for any degree or diploma in this university or any other institution.

__________________ __________________

Anioke Chisom N. Date

We certify that this project has been successfully defended and accepted for the award of the degree of B.Sc in Banking and Finance.

Mr. Nwadiubu Anthony	____________	____________
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(Head of Department)	Signature	Date
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(External Examiner)	Signature	Date

DEDICATION

This research work is dedicated to the Almighty God, whom through him, all things were made possible.

And finally, my loving parents, Chief and Mrs. Anioke O.O.

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ABSTRACT

This research work was undertaken to assess the Loan granting and its recovery problems on Commercial Banks. The research was intended to achieve the following objectives: To find out the several problems facing loan recovery, the effects of loan default on commercial banks and the measures that will be used in reducing the incidence of loan default. Relevant data were collected from both primary and secondary sources. Questionnaires were the main primary data collection instrument employed while data from various relevant publication constituted the sources of secondary data. Upon the analysis of data, the following conclusions were drawn: That problem of loan default stemmed from the fact that there is unavailability of security to be disposed by banks to realize funds. And also customer's attitude towards loan payment. On the basis of the above findings, it was recommended that commercial banks should use some risk control measures to guide against loan default. Also, before granting loan, they should examine critically the project statement submitted by the customer or borrower which will help them to find out the realistic repayment pattern and also help them in knowing if the projects are realistic based on the customer's past performance. Also, the Central Bank of Nigeria should create a conducive environment for the successfully operation of commercial banks in Nigeria.

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CHAPTER ONE

1.1 BACKGROUND OF THE STUDY:

Virtually, every business has a credit relationship with a financial institution, especially banks. Some rely on periodic short term loans to finance temporary working capital needs. Others primarily use long-term loans to finance capital expenditure, new acquisitions or permanent increases in capital. Regardless of the type of loan, all credit request mandate a systematic analysis of the borrower's ability to repay as at when due.

Commercial banks carry on ordinary banking business with the general public, changing cash for bank deposits and bank deposits for cash, transferring bank deposit from one corporation to another, giving bank deposit in exchange of bills of exchange, providing of trustees and executor's services, providing safe custody of funds and valuables as well as foreign exchange remittance.

Though commercial banks differs from country to country, their profit and banking motives are the same. Their activities are of interest to their customers, workers (staff), and above all, shareholders. The commercial objective of the bank is to maximize profit, though other social and economic functions tends to deflect banks from profit maximization.

The aims and objectives of commercial banks have therefore paved way for their customers to make and obtain credits, in form of loan of which the researcher is interested in.

Lending has become a vital function on operation because of its direct effect and impact on economic growth and business development.

In a market oriented economy, there are two main participants that move the economic growth; these are the suppliers of invisible funds and the users of the funds for productive purposes. These two participants are spread widely in the economy and may not have direct relationship with each other. For this, there is the need to have an intermediary to link them up. The banking sector mobilize surplus funds from small and big savers who have no immediate need for such funds. The users of these funds are the business entrepreneurs and investors who have brilliant ideas on how to create additional wealth in the economy but lack the necessary capital to execute their ideas. These groups of people approach banks to obtain loan.

Subsequently, lending is a risky venture which banks only engage on after a rigorous and satisfactory analysis of the project for which lending is being made. The main preoccupation of banks is extending loans to their customers. Thus, the formulation and implementation of such lending policies are some of the important responsibilities of the management of the bank. The lending policy of a bank must be specific on how much loan will be made available to whom, what period and for what reason. For this reason, lending policies should be well documented so that lending officers will be able to know the areas of prohibition and the area of where they can operate. Also, such policies should be subjected to periodic review to make the banks keep abreast with the dynamic and innovation nature of the economy as well as competing with other changing economic sector.

Therefore, the basic objectives of credit analysis t=is to assess the risks involved in extending loans to bank customers. In financial circle, risk typically refers to the volatility in earnings. Lenders are particularly concerned with adverse fluctuation in net income or cash flows, which hinder the borrower's ability to service a loan. Some risks can be measured with historical and projected financial data, while others such as those associated with borrower's character and willingness to repay a loan are not directly measurable.

1.2 STATEMENT OF PROBLEMS:

Banks in recent times has failed as a result of loan recovery problems. Loan is the major source of bank profitability.

However, in going about their lending activities, banks have their own objectives among which are profitability, growth, safety, suitability and liquidity.

Loan, when not recovered could adversely affect banks. It is easily granted than recovered. It usually needs proficiency i.e. competency and expertise in the recovery process. It sometimes become an uphill task to recover. When they are not recovered, the impact is often disastrous to the bank. It can lead to illiquidity, insolvency and even distress as the case may be.

There is therefore a need for arriving at strategies for efficient loan recovery. That is the peak of the problem.

1.3 OBJECTIVES OF THE STUDY

Having known that lending objectives of a commercial bank is to provide growth, profitability and liquidity, and its representing chunk of deposit as a source of income to the bank, the cumulative effect of loan default will be a loss of confidence in the banking system.

The researcher therefore aimed at:

1. Finding out the several problems facing loan recovery
2. The effects of loan default on commercial banks
3. The measures that will help to reduce the incidence of loan default.

1.4 RESEARCH QUESTION

1. What are the several problems faced during loan recovery?
2. What type of loan do commercial banks grant?
3. Who are the loan beneficiaries of commercial banks?
4. Are there measures to reduce the limit of loan default?
5. What are the effects of loan defaults on commercial banks?
6. What are the sectorial allocation of commercial bank's loan?
7. What are measures that will help to reduce the incidence of loan default?

1.5 RESEARCH HYPOTHESIS

Ho – the measures taken by banks do not reduce the incidence of loan default.

H_1 The measures taken by banks to reduce the incidence of loan default

1.6 SCOPE OF THE STUDY

The research work is to analyze the problems of loan recovery on commercial banks (First Bank Plc) in Ojo-Alaba, Ojo Local Government Area of Lagos State.

Due to limited time and the level of this project work, the researcher decided to systematically and meticulously narrow it down to a study that will cover two distinct areas namely:

The problem of loan recovery and how to control loan default.

The researcher wants to avoid unnecessary details that are not concerned with the problem of loan recovery in commercial banks.

The study is limited to first bank branch in Ojo-Alaba, Lagos State.

1.7 SIGNIFICANCE OF THE STUDY

This study is intended to analyze the problems of loan recovery in commercial banks in Nigeria and their poor system of management of loan. The result of this study will be immense important to some of us and even the bankers in particular. Banks will become conscious in their loan disbursement. They have to determine the kind o people that will benefit from the loan disbursement, the type of loan to give the criteria to use in granting loan and the procedures to be used for loan recovery.

1.8 DEFINITION OF TERMS

In the course of the study, the researcher makes use of some words that needs to be defined so as to carry the reader along.

LOAN: This is the act of allowing a borrower to make a temporal use of funds at its disposal. It is also a more formal arrangement by which a bank agree to lend an agreed amount to a customer usually for a given period.

RISK: It is the measure of uncertainly inherent in any decision making process.

PROFITABILITY: It is used as index for measuring managerial performance. It means yielding or bringing profit or gain.

LIQUIDITY: This is the word that banks used to describe their ability to satisfy demands for cash in exchange for deposits.

BANKING: It is an agency through which debts and credits are converted and exchanged between owners.

BAD AND DOUBTFUL DEBT: Bad debts are those which are not recoverable, though they are written off as loss. Doubtful debts are those of which the recovery in full or part is uncertain.

CAPITAL: It is the equity value of the bank educated to the present value of its future earnings.

1.9 LIMITATIONS OF THE STUDY:

In the course of the study, the researcher was faced with several constraints. One of the constraints was the short time period within which the research was to be completed. Another factor was shortage of cash which prevented the researcher from traveling to source the data. Also, most of the credit analysis criteria in commercial banks were not disclosed to offer the necessary data required. Their frequent postponement of appointment coupled with the fact that commercial banks in Nigeria are vast in population i.e. First Bank Branches. The researcher could not get to all of them, therefore a sample was taken to represent all.

CHAPTER TWO

LITERATURE REVIEW

2.1 BRIEF INTRODUCTION

Banking literature is generally full of research findings relating to the objectives of banks with that of their customers, staffs and shareholders. There is no literature dealing extensively on the problems of loan recovery on Nigeria commercial banks.

However, a close examination of some scholars on related topic exist. Most of them try to attribute this problem to poor debt management which result to most bad debt.

In accordance with the words of Ralph K.O Osayemeh, (1998) "*Lending decision*" P.23, "Very much like investment decisions are generally full of risk but the ability to banks to thoroughly assess and analyze such risk will lead to qualitative and more pragmatic decision”.

Lack of adequate knowledge of the loan sector could result to most bad debts and moreover, the success of most loan depend on the perfect assessment of the customer’s character.

If the customers are introduced by another customer, the market fairly becomes simpler because the introducer may often guarantee on behalf of the new customer. He suggested that loan for speculative business should not be granted even if it is fully supported by collateral. Here, possibility of default is high. Emekekwe Patrick, (1994) P.P 65.

Akuakaelem Maria .M. (2000), in her contribution enumerated some of the causes of loan default as decline in business, abandonment of account, delay in project completion, diversion of funds and increase in interest rate. Also bad debt in lending are caused by highly defective loan administration operations at the bank which stem from the over bearing influence of directors who relegates central rules in favour or personal and political interest by virtue of the nature of appointments.

Other attributes to the cause of these bad debts are improper documentation, insufficient security, unstable economy, customer’s dishonesty, loopholes in legal handlings and improper perfection of security documents.

2.2 THE NATURE OF LOAN AND ADVANCES GRANTED BY BANKS

Bank loan can be classified in various ways according to the class of people the loan is granted to. Thus, loan can be classified according to purpose namely:

1. Personal loans
2. Agricultural loans
3. Bridging loans
4. Industrial loans
5. Probate loans

Loan as well can be classified based on the period of maturity. From this, we therefore have short, medium and long term loan. The short term loan does not exceed one year. Medium term loan last for only two to three years. While long term loan last for about five years.

1. **Personal Loan:**

This loan is normally for durable customer goods, repair and decoration, rents, school fees, house renovation, purchases of car or other personal consumption or investment items. Such loan are usually for small sums and are often referred to as petty lending.

The banker must find out the purpose of the loan through discussion with the loan seekers, how much is needed by the customers and whether repayment could be made without much stress on the customers or the bank either. The net monthly income is computed while the monthly expenses is deducted to assess the available disposal income from which the loan can be repayed. The reason for calling the “personal loans” is because they are normally granted to enable individuals to purchase consumer durable good, e.g. motor cars, television sets etc.

Usually, security is not required for this type of loan. As frequently, this is built into the loan agreement as an insurance against non-payment, should the borrower die before repayment? Interest is charged ‘up front’, that is, when the loan is granted. Thus, interest is added to total amount which is repayable. This means that the interest is charged on full amount over the total period. As a result, the customer is repaying the capital in regular installments, which means that each month, the debt due to the bank is being reduced, yet the interest charged is on the full amount for the whole period which makes the interest charged penal.

Once interest is fixed, the customer can be at a disadvantage if interest rates are reduced rationally. Alternatively, if during the life of the loan, interest rates are increases, he may benefit.

2. **Agricultural loan:**

The agricultural sector plays a major role in the economic development of any country. Funds are disbursed on both short and long-term basis for the purchase of seed, fertilizers, machinery, cattle etc.

Banks normally refuses agricultural loan because of its long gestation period and also because of poor harvest on account of weather influence. Also, the fact that farmer direct the loan for other purpose such as increase in the number of their wives in order to encourage banks to go into agricultural finance which is considered the agricultural credit guarantee scheme in 2000.

In the 2002 budget, government promised to give subvention to states and to ensure that the federal government concentrated on agricultural planning.

Nigerian Agricultural and Co-operative Bank (NACB) plays a major role in agricultural loan disbursement. If necessary, some forms of security are obtained.

3. Bridging Loan:

When house-owners require temporary finance in order to purchase a property at the same times as selling the house in which they live, it is often the bank that provides finance to purchase the new property and receives repayment when the old property has been sold. When this type of loan is required, the bank likes to see that the completion date of the sales and purchase contracts are known as they have a solicitor's undertaking that the proceeds of the sale will be delivered to the bank.

It is on rare occasions that the bank will give an 'open ended' bridging loan, which is a loan to cover the purchase of a property before the first property is sold. Bridging loans are, from the bank's point of view, simple profitable and self-liquidating.

4. **Industrial loan:**

Moratorium is given under this loan which the customer is given time to set up and yielding before repayment is commenced.

Industrial loan repayment normally depends on the production or survival of the company. If it cannot achieve its optimum production, the tendency to repay loan is doubtful.

5. **Probate loan:**

A probate loan is granted to an executor of a will when, in order to obtain probate (i.e. the transfer of the deceased's assets to the executor), capital transfer tax must be paid. The executor needing funds will go to the bank, show the manager evidences of his right to the executorship, a loan will be granted and the tax paid when probate is then granted. The loan is either repaid from the deceased's current/deposit account, or if this is insufficient, an asset –say stock and shares is sold to repay the loan.

2.3 PROBLEMS OF LOAN DEFAULT

Loans are classified as problem credits when they cannot be repaid. Problem loans and losses essentially reflects the difficult risk inherent in a borrower's ability and willingness to repay all obligations. The lending process by its nature is imperfect. Credit analysis may be incomplete or based on faulty data. Loan officers may ignore the true condition of borrowing with strong personal ties with the bank, and a borrower's ability to repay may simply change after a loan is granted. If management concentrates solely on minimizing losses, a bank will make virtually no loans; profit will shrink and the legitimate credit needs of customers will not be met. Lenders cannot completely eliminate risks, so more loan losses are expected. The objective is to manage losses well so that the bank can meet its risks and returns targets. John Orjih, (2002:65).

Loan defaults arise as a result of debts due to creditors but for some inherent weakness, the full or partial recovery is considered impossible. From the banker's point of view, loan default (bad debt) are components of accounts receivable or credit granted to the customers of the bank but which cannot be recovered within the specified period, for one reason or the other.

2.4 CAUSES OF LOAN DEFAULT

Loan defaults are caused by variety of factors, some controllable and others uncontrollable. Controllable factors are those that reflect overall bank credit policy as well as inadequate credit analysis, loan strutting and loan documentation. Uncontrollable factors typically reflect adverse economic conditions, adverse changes in regulations, environmental changes surrounding the borrower's operations and catastrophic events. While there is little that can be done to prevent uncontrollable variables. Effective credit granting procedure can significantly reduce other sources of looses.

The following affects loan default's

1. Bank-related factors
2. Customer-related factors
3. Uncontrollable factors

1. Bank-related factors:

a. Lack of in-depth knowledge of Customer's Operation: Some banks grant credit to customers based on hazy knowledge of customers operations and personality. This practice usually leads to situations whereby loans are granted to customers who have neither the willingness nor the capacity to repay the loan.

B. **Excessive dependence on financial statements:** The information contained in the financial statement of the customer serves as a tool for proper loan administration. The loan administrator should not work on the statements on their face value, neither or rather in-depth financial analysis of the data is required for sound decision-making.

C. **Connected lending:** Some lending officers in the bank provides loans to their relations or related business without considering the basic principles of lending. This practice often leads to bad and irrecoverable debts of loans.

D. **Lending on over valued securities:** Often times, the securities deposited with the bank are not properly valued to reflect the current market prices. These securities are over valued and even when they are realized; they do not cover the value of the loans.

E. **Inadequate project monitoring:** Incidences of bad and doubtful debts in banks may be as a result of inability to monitor and recover their loans due to lack of swell articulated and communicated loan policies to guide lending operations.

F. **Inadequate knowledge of project appraisal techniques:** In some banks, some lending staffs are not academically and professionally knowledgeable to appraise projects properly. Consequently, most loans granted by them becomes irrevocable.

2. Customer-related factors:

Most business failures result from management expertise, inadequate planning and accounting systems, outright fraud and general incompetence. In many cases, the original founder of a company is unwilling to relinquish any responsibility to subordinates. As the company grows, the founder does not have sufficient expertise and time to handle all operational details. Because all key decisions are centralized, the firm does not react quickly to changing market conditions and does not generate new product ideas. Many companies simply outgrow their existing management skills, which are limited in the areas of accounting, finance and marketing.

b. Inadequate initial capitalization: Some business often run into problems shortly after beginning operations because of inadequate capitalization. Owners underestimate the costs of opening the doors for business and overestimate the speed with which they can turn out profit. By the time they recognize the problem, their capital had depleted and lenders refuse to extend additional credit.

c. High financial and operating leverage: If a company has a large amount of outstanding debt and the high percentage of its total costs are fixed it operates with a high degree of financial and operating leverage. High financial leverage exposes the firm to high interest payments that must be met when sales decline. High operating leverage exposes the firm to substantial depreciation and maintenance expenses when sales decline. In both cases, the volatility of earnings is high relative to changes in sales.

d. **Misconception of bank loans:** Some borrowers do not clearly understand the purpose of bank loans. They sometimes regard bank loans as windfall receipts and very much unwilling to refund them.

e. **Strong Competition:** To grow and remain profitable, companies must adapt to economic events. They should regularly improve existing operations and introduce new products to remain competitive. Frequently, new competitors move into a firm's market and disrupt normal operations.

A company can react either offensively or defensively. Offensive responses normally focus on marketing efforts intended to differentiate the firm's products and segment the market. In many cases, the firm cuts prices to retain market share and may not break even.

f. **Loan Diversion:** Diversion of loans purposes other than those for which they are granted most often leads to bad debt. This is because the expected cash flow cannot be granted to meet up repayment schedule.

3. Uncontrollable factors

a. Economic downturn

Many firms cannot operate profitably in a declining economic environment.

Their costs may be fixed because of high leverage, and their sales may deteriorate if they are not the market leaders. The resulting strain on cash flow impairs the firm's ability to repay their loans.

b. Changes in economic policies:

Changes in economic policies may affect the operations of a borrowing firm, and consequently the ability to honour loan obligations.

c. Changes in taste and preference:

The customer's ability to service and repay loans may be adversely affected by shift of consumers taste away from his products. This entails decline in sales, fall in revenue and inability to refund loaned funds.

d. **Natural Hazards:**

Some hazards, such as wars, desert encroachment, locust invasion, fire, flood etc may affect the borrowers' capacity to repay the loan as and when due.

2.5 EFFECTS OF LOAN DEFAULT:

The lending of funds deposits with banks to those who require them implied risk taking by the lending credit may not materialized as planned. The lending institution demands may be made by depositors.

If this happens, the lending institution would not be able to attain the objectives expected of them. The overall effect would be a loss of confidence in the banking system.

Other negative effects of default on loan repayments are :-

1. **Loss to banks:** The un-recovered loans constitute a very heavy loss on the part of the banks. When the debts are not paid, the banks have to write them off which sometimes have significant adverse effects on the banks operations.
2. **Decline in revenue:** The interest loss adversely affects the bank's major revenue. The main activity of the banks is the granting of loans and credit to customers. They charge interest on loans and this forms a major source of revue for them. Failure to pay interest on loans means that the banks will loose substantial revenue.
3. **Distress:** In a situation where bad accumulate largely to the extent that the bank cannot write them off, it may lead to the bank becoming illiquid. After this stage, if the situation does not improve, the affected banks may become distressed and ultimately go into liquidation.
4. **Increased overhead:** When the debt foes bad, the bank may resort to legal action to receive part or the whole of the debt. The legal fee involved in most cases is usually very enormous. Regrettably, they may lose the case after spending the huge amount on litigation.
5. **Limited Credit Creation Capacity:** As bad debt increase, the capital of the

bank decreases and the money available to the banks for lending becomes depleted, thereby hampering the capacity of the banks to create credit.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 RESEARCH DESIGN

The research design used for this work is survey design. Here, group of people were studied by collecting and analyzing their data. These group of people were selected from the population to represent the population sample.

This is a field survey type of research, supported by library research work.

relevant questions.

3.2 DEFINITION OF POPULATION :

Presently, at the time of this research work, there exist about two first bank branches in Ojo-Alaba. Out of the two branches, one was chosen which automatically form the population of the study.

The population of the study is one hundred staff which forms the population of the study.

3.3 SAMPLE SIZE

The sample size will be obtained using the Taro Yameni formular stated below;

$$n = \frac{N}{1+N\,(e)^2}$$

Where,

n = sample size

N = Population size

e = level of error

I = Mathematical constraint

The level of error of 0.05 was chosen by the researcher.

Therefore;

$$n = \frac{100}{1 + 100\,(0.05)^2}$$

$$n = \frac{100}{1.25} = 80$$

$$n = 80$$

3.4 SOURCE AND METHOD OF DATA COLLECTION

Information were gathered through primary and secondary source of data collection. The primary source constituted the major source due to the responses to the questionnaire that was distributed to the staff of the bank.

The secondary source were from textbooks, journals and write ups of some scholars. The method of data collection was structured questionnaire which were distributed to the staffs of the bank to get at facts and figures as regards to the nature of the loan granted, the number of loan beneficiaries and the number of loan defaults, those that pays promptly and other relevant questions.

CHAPTER FOUR

4.0 DATA PRESENTATION AND ANALYSIS

As already mentioned in chapter three of this work, the researcher used some methods in the cause of carrying out this research.

These includes: questionnaire, tables, figures and percentages. All these helped to reduce sampling error and bias in writing the project.

4.1 PRESENTATION AND INTERPRETATION OF DATA:

Here, the researcher assembled, presented and analyzed the relevant data gathered. Structured questionnaire were distributed to the staff of the bank. Only the branch manager, accountants and top officials of the bank, including other staffs of the bank were chosen to fill the questionnaire. It is from the information from the respondents, that the analysis was made possible. It should be noted also that the bank's system of classifying the nature of loans and loan beneficiaries are to be used in this analysis. The researcher at this point starts to present the data.

QUESTION 1

What type of loan do you grant?

Table 4.1

Responses	Number	Percentage (%)
Short-term	60	75%
Medium-term	20	25%
Long-term	0	0
Total	**80**	**100**

Sources: Field survey 2012

Table 4.1 depicts that 60 respondents or 75% of the sample size agreed that the bank grants short-term loan. 20 respondents or 25% of the sample size said that the bank grants medium-term loan while nobody said that the bank grant long –term loan.

QUESTION 2

What is the sectorial allocation of your loan?

Table 4.2

Responses	Number	Percentage (%)
Agricultural loan	10	12.5%
Industrial loan	40	50%
Personal loan	20	25%
All of the above	**10**	12.5%
Total	**80**	**100**

Source: filed survey 2012

Table 4.2 depicts that 10 respondents said that they grant agricultural loan. 40 respondents of the sample size said that they grant industrial loan while

20 respondents of the sample size said that they grant personal loan. Only 10 grants all.

QUESTION 3

What are the several problems faced during loan recovery?

Table 4.3

Responses	Number	Percentage (%)
Customer unable to pay	10	12.5%
Lack of collateral	20	25%
Inability to arrest customer	40	50%
All of the above	10	12.5%
Total	**80**	**100**

Sources: Filed survey 2012

Table 4.3 shows that all the respondent said that they faced the problem of lack of collateral, customers unable to pay or repay loans during loan recovery and inability to arrest customers.

QUESTION 4

Who are your loan beneficiaries?

Table 4.4

Responses	Number	Percentage (%)
Sole traders	10	12.5%
Partnership	20	25%
Limited Liability Company	40	50%
All of the above	10	12.5%
Total	**80**	**100**

Sources: Field survey 2012

The above table depicts that 80 respondents or 100% of the sample size said that all the parties listed above benefits from loans granted by the banks.

Questions 5

What are the effects of the defaults?

Table 4.5

Responses	Number	Percentage (%)
Sole traders	10	12.5%
Partnership	20	25%
Limited Liability Company	40	50%
All of the above	10	12.5%
Total	**80**	**100**

Sources: Field survey 2012

The above table stated that 10 respondents' states that default on loan repayment causes distress on bank, while 40 said that defaults cause liquidity on banks, 20 responded that it brings about reduction on bank's loanable funds and 10 responded that the above listed points are the effects of defaults in repayment of loan.

Questions 6

Are there measured to reduce the limit of loan default?

Table 4.6

Responses	Number	Percentage (%)
Yes	80%	100%
No	0	0%
Total	**80**	**100**

Sources: field survey 2012

The above table states that 80 respondents said that there are measures to reduce the limit of loan default. This represents 100% of the sample size.

Question 7

Who are the greatest defaulters of loan repayment on commercial

banks sectorial allocation?

Responses	Number	Percentage (%)
Agriculturalists	10	12.5%
Industrialists	15	18.7%
Individual (personal)	5	6.3%
Corporate enterprises	50	62.5%
Total	**80**	**100**

Sources: Field survey 2012

Table 4.7 depicts that 50 respondents or 62.5% of the sample size agreed that corporate enterprise are the greatest defaulters of loan repayment.

Table 8

What sector of bank's loan allocation have the highest rate of loan repayment?

Responses	Number	Percentage (%)
Agriculturists	10	12.5%
Industrialists	15	18.7%
Individual (personal)	50	62.3%
Corporate enterprises	5	6.3%
Total	**80**	**100**

Sources; field survey 2012

Table 4.8 depicts that 50 respondents or 62.5% of the sample size agreed that individuals have the highest rate of loan repayment.

Question 9

What are the measures that will help to reduce the incidence of loan default?

Responses	Number	Percentage (%)
Demand notice	10	12.5%
Taking legal action	40	50%
Realizing the security	30	37.5%
Total	**80**	**100**

Sources: Field survey 2012

Table 4.9 depicts that respondents or 12.5% of the sample size agreed that demand notice is the measure that will be used to reduce the incidence of loan default. 40 respondents or 50% of the sample size said that taking legal action will be used to reduce the incidence of loan default. While 30 respondent or 37.5% of the sample size agreed that realizing the security will also help in reducing the incidence of loan default questionnaire. The relevant answer will be considered in order to determine the causes of variation in individual bank's operations.

4.2 DATA ANALYSIS FINDINGS:

The researcher have so far tried to make a combined analysis given by the banks to the question asked. Most commercial banks grants short-term loan. Their major beneficiaries include sole proprietors, partnerships and corporate enterprises.

It was also discovered that there has been default on loan repayment. The major effects these have on banks is that the loanable fund is reduced to minimum. And this affects the lending capacity.

4.3 DISCUSSION OF THE FINDINGS:

In the course of the research work, the researcher also discovered other things, which have the need to unravel in order to give a clear picture of what is going on in banking industry. The individuals have the highest rate of repayment. This is because the burden of court actions or sales of their properties fall on the individuals. To avoid greater loss, they have to comply whenever there is threat on them. A close examination of the loan beneficiaries reveals that the corporate enterprises have the greater percentage of defaulters and this is due to the following:-

- They receive the amount of loan which attracts huge interest.
- There is dynamism in monetary policy which have the effects of disrupting the original repayment plan.
- Inefficient management

Agriculturalist default due to the reason that the loan has a very long gestation period. This means that it takes time for the loan to mature, something can happen along the line that could prevent repayment.

Industrialists default because at times infant industries may not survive due to internal management problems. Where the industry cannot attain optimum production, it will not be able to pay/repay. Industrialists at times do not value these loans and as such do not invest them in profit making ventures.

4.4 RECOVERY MEASURES:

Several steps were taken by banks in recovering their loan from the defaulters. These steps are:-

1. **Demand Notice:** The customer is notified in writing, calling his attention to the agreement. If the customer fails to respond to the first letter, a reminder may be sent.

2. Realizing the security: In the worst circumstance where the business is beyond redemption, the banker must minimize any looses by disposing the collateral.

The ability of the banks to dispose the collateral on their own immediately depends on whether they obtain a legal mortgage; otherwise they cannot sell of the collateral without obtaining a court sanction.

3. Take legal action: Before instituting legal action, the legal department or the external solicitor will issue strongly worded demand to the customer asking for the repayment.

If after 14 days, and the debtor fails, then the solicitor will go to court on his client's behalf. If judgment against the debtor is obtained, then the bank's claim is established and the extent of his customer's liabilities on the debt determined.

Very often, the court gets debtors committed to a specified repayment proposal for the judgment debt including cost awarded. Where the debtor default on the repayment proposal confirmed at the judgment, the solicitor may obtain a garnishee order.

By garnishee order, the movable property does not fully satisfy the department, the solicitor may apply to the court for an order enabling him or her to take possession of the immovable property to be auctioned by the bailiff for satisfaction. Any surplus will be returned to the judgment debtor.

This is done as a last resort because it is cumbersome, time consuming and expensive and also because it represent a sad way to terminate what probably was an interesting banker-customer relationship.

Hypothesis 1

Ho: The measures taken by banks do not reduce the incidence of loan default.

H_1: The measures taken by banks do reduce the incidence of loan default

Data of responses

Variable	No of responses	Percentage
Demand notice	10	12.5
Taking legal actions	40	50
Realizing the securities	30	37.5
Total	80	100

Sources: Survey data 2012

Depicts the respondents or 12.5% of the sample size agreed that demand notice is the measure that will be used reduces the incidence of loan default. 40 respondents or 50% of the sample size said that taking legal action will be used to reduce the incidence of loan default while 30 respondent or 37.5% of the sample size agreed that realizing the security will also help in reducing the incidence of loan default questionnaires.

Chi square table

Variable	0	E	(o-e)	$o-e^2$	$(o-e)^2/_e$
Demand notice	10	10	0	0	0
Taking legal action	40	50	-10	100	2
Realizing the securities	30	20	10	100	5
Total	80	80	0	0	7

Computed value of $x^2 = \Sigma\ (o-e)^2/e$

Degree of freedom = (R- 1) (C-1)

= (2-1) (3-1)

= 2

Level of significance = 0.05

X^2 distributions (2, 0.05)

The table value of X^2 is 5.991.

Decision Rule

If the computed value of X^2 ‹ than the table value of X^2 accept the Ho hypothesis and reject H_1 hypothesis but if the computed value of X^2 › than the table value of x^2 reject the Ho hypothesis and accept the Hi hypothesis which means that there are measures that will reduce the incidence of loan default.

HYPOTHESIS 2

Ho: Loans to individuals do not record higher rate of loan default.

H1: Loans to individuals record higher rate of loan default repayment.

Data of hypothesis

Variable	No of responses	Percentage
Agriculturists	10	12.5
Industrialist	15	18.7
Individual	50	62.5
Corporate enterprises	5	63
Total	80	100

Sources: Survey data 2012

The table depicts that 50 respondents or 62.5% of the sample size agreed that individual have the highest rate of loan repayment.

Chi square data of hypothesis

Variable	0	E	(o-e)	$o-e^2$	$(o-e)^2/_e$

Agriculturist	10	10	0	0	0
Industrialist	15	5	-10	100	1.667
Individual	50	60	10	100	6.667
Corporate bodies	5	5	0	0	0
Total	80	80	0	0	8.334

Sources survey data 2012

Computed value of $x^2 = \Sigma (o-e)^2/e$

Degree of freedom = (R- 1) (C-1)

= (2-1) (3-1)

= 3

Level of significance = 0.05

X^2 distributions (3, 0.05)

The table value of X^2 is 7.826.

DECISION RULE

If the computed value of X^2 ‹ than the table value of X^2 accept the Ho hypothesis and reject H_1 hypothesis but if the computed value of X^2 › than the table value of x^2 reject the Ho hypothesis and accept the Hi hypothesis which means that there are measures that will reduce the incidence of loan default.

CHAPTER FIVE

SUMMARY Of FINDINGS, RECOMMENDATION AND CONCLUSION:

5.1 SUMMARY OF FINDINGS:

This study has a large extent attempted to analyze the loan granting and its recovery problems on commercial banks. The objective was to find out the problems encountered by commercial banks during loan recovery.

In this regard, the research questions were able to embrace the nature of the loans granted as well as the effect of the default. The major causes of these problems as analyzed could be classified into:

a. Adversity

b. Mismanagement

c. Fraud

Lending, being a vital function in banking operation is no longer what it use to be. This is because lending entails a lot of risks on the part of the lending banker. The lending policies are no more strictly adhered to. The issue of loan recovery problems arises when the repayment of the granted loan does not follow as planed and agreed. And if not properly checked, it will have an adverse effect on the operations of the commercial banks and will pose a threat to their expectations.

However, at the end of the study, the following observations were made:

1. Most banks grant short-term loans

2. Banks does no accept only collateral affected by the defaults.
3. Banks have been seriously affected by the defaults
    4. Banks are not idle but have applied tactical recovery measures
    5. Some of the measures are effective

5.2 RECOMMENDATIONS

If all lending application could be modified and the risk elements qualified, lending could be done by computer but as any banker should know, lending is the 'fun' and 'leaves' dangerous element in banking this is because no matter how careful banks may be, they must still expect some of these loans to turn bad debts. Therefore, once a loan is identified as a problem, commercial banks are faced with how to avoid possible loss. And to achieve this, the following recommendations were made:

a. Commercial banks should monitor its outstanding loans in order to identify promptly loans which a borrower fails to repay as scheduled.

b. Commercial banks should use some of the risk control procedures to guide against losses. An example of this is covenant which is a written agreement whereby the borrower commits himself of providing specific financial statement at specific intervals during the life of the loan.

c. Compensating balance: This is a system under which the borrower agrees to maintain specific level of deposits at the lending bank. If the borrower defaults, then the lending bankers use its right to off-set the borrower's loan with the deposit at the bank.

d. Before granting loans, commercial banks should examine critically the project of financial statement provided by the customer (cash budget, income statement). This will help them find out the realistic repayment pattern and also help them I knowing if the projects are realistic based on the customers past performance.

e. The government should educated on the need to repay loans.

f. Collateral to be accepted should have higher marginal values, considering the inflationary situation in the economy. Also, effort should be made to ensure that the furnished collaterals are existing. This is so because some dishonest customers will believe that there is collateral of which it does not exist.

5.3 CONCLUSION

The researcher wish to conclude by saying that risk in credit creation through loan granting cannot be completely wiped out because of the futuristic nature of loan repayment schedule.

Most of the loans granted by Nigerian Commercial Banks do not get repaid and turn out to be bad debts.

THE REASONS FOR SITUATION ARE:

1. **No security to dispose and realize fund:** Some of the bank loans have no collateral pledged against them. Consequently, if such beneficiaries default, there will be no security to dispose off and recover at least part of the loan.

2. **Peoples' attitude towards loan payment:** Some people (borrowers) take loan to be national gifts from the government and as such, they do not repay them. Banks do not down to watch the defaulters. They make serious effort to see that they recover those loans.

   Finally, it is time that the banks do provide bad debts, doubtful debt etc. This is done to ensure adequate protection for the size of credit portfolios rather than a reflection of actual losses to the banks.

5.4 SUGGESTION FOR FURTHER RESEARCH

The researcher undertakes to study loan granting and its recovery problems on commercial banks with the view of finding out the several problems faced during loan recovery, the effects of loan default on commercial banks as well as the measures to reduce the limit of loan defaults. However, the researcher does not find out the way the commercial banks mobilize these loanable funds that they extend to people and hence from the basis for further research.

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APPENDIX A

Department of Banking and Banking
Finance,
Caritas University,
P/M/B/ 01784,
Amorji-Nike
Enugu.
5th of December, 2008.

Dear Respondents,

Questionnaire on "Loan Granting And Its Recovery Problems On Commercial Banks".

I am currently conducting a research work on the topic "Loan granting and its recovery problems on commercial banks. This is for the partial fulfillment for the award of Bachelor of Science Degree in Banking and Finance.

This is purely for academic exercise and the data collected shall be strictly and confidentially used for the purpose for which it is designed. This questionnaire is meant for managers, accountants, and other officials of the bank.

Thanks for your co-operation.

Yours faithfully,

Anioke Chisom

APPENDIX B

Name……………………………………………………………………………………

Occupation……………………………………………………………………………

Marital

Status…………………………………………………………………………………

Sex……………………………………………………………………………………

INSTRUCTION

Please tick X where necessary in the boxes.

QUESTIONNAIRE

1. What type of loan do you grant?

a. Short-term

b. Medium-term

c. Long-term

d. All of the above

2. What is the sectorial distribution of your loan?

a. Agricultural loan

b. Industrial /Commercial loan

c. Bridging loan

d. All of the above

3. Who are your beneficiaries?

a. Sole traders

b. Partnership

c. Limited liability companies

d. All of the above

4. What are the several problems faced during loan recovery?

a. Customer's inability to pay

b. Lack of collateral to fall back on

c. Inability to track down customers

d. All of the above

5. Must there always be collateral securities before loans are granted?

a. Yes

b. No

6. Have there been defaults in loan payment for the past five years?

a. Yes

b. No

7. What reasons could be attributed to the defaults?

a. Fund diversion

b. Dishonesty

c. Poor financial analysis

d. All of the above

8. Which of these have more frequency of defaults?

a. Agricultural loan

b. Industrial loan

c. Bridging loan

d. Personal loan

9. What are your strategies?

a. Persuasion

b. Court Jurisdiction

c. Disposal of collateral

d. Personal loan

10. What is the limit of effectiveness of the strategies?

a. Very effective

b. Effective

c. Not very effective

d. All of the above